Some differences between project management and accounting perspectives on project cost control

By Alan Stretton

ABSTRACT

This short commentary discusses some differences in perception and practice between project managers and accountants in relation to cost and financial management of projects.

Conventional accounting records incomes and expenditures as they pass through the accounting books. From the point of view of project financial and cost control, this does not, in itself, provide a basis for cash flow control, nor for some aspects of cost control.

The facility to forecast future cash flows and future costs is required, and this is best catered for by having a separate project control system which facilitates such forecasting. This is often resisted by accountants, until (or if) the logic and means of reconciling it with conventional accounts is accepted.

This article discusses aspects of such a separate control system, including commitment costing for procurement items, and use of a specifically detailed WBS for dealing with the percentage complete problem for non-procurement items.

INTRODUCTION

This commentary discusses some of the issues I have experienced over the years in reconciling differences in perspectives between accountants and project managers regarding cost and financial management of projects.

Project managers and accountants tend to have quite different perceptions of what is important in the context of project cost and financial controls. These are what I have called (e.g. in Stretton 2013c) legitimately conflicting perceptions, in the sense that both are right in respect of their own particular responsibilities. If each understands the legitimately different perspective of the other, then working smoothly together becomes much less of a problem. It has often been my task to explain project management perspectives to accountants, and to involve them in incorporating these into expanded formal financial and cost control systems. The following reflects on some of these differences of perspectives.

DIFFERENCES RE PROJECT COST AND FINANCIAL CONTROL

Traditional accounting processes record incomes and expenditures at the times they actually pass through their books. This is fine as a basis for recording cash flows, and as a basis for controlling some aspects of project costs, particularly if recorded expenditures are close to being current. However, on their own they are quite insufficient to achieve effective project cost control. As noted in the abstract, the capability to forecast future cash flows and costs is required for adequate control, and this is best accommodated by a separate project control system which facilitates such forecasting capability.

I discussed the latter in some detail in Stretton 2009f, and now summarise some of the factors in that paper which are relevant to different perceptions of accountants and project managers on this topic.

Project procurement items – commitment costing

When a project places a procurement order (for materials, sub-contracts, etc) for an agreed amount, it has, in effect, made a commitment to pay that amount at some time in the future. As such, this should be registered as a committed cost as soon as the order is placed, as if the money had already been spent. This is an important component of a separate project control system that focuses on forecasting future costs.

The reason for needing a separate project cost control system for procurement items is rather obvious. Conventional financial accounting systems only register incurred cost after delivery of procured items and presentation and payment of corresponding invoices or progress payment claims. Historical recording of cash out is little help in these circumstances. Commitment costing records the commitment at the time the order is placed. If there are reasonable doubts at that time about the eventual cost, the project manager then adds a contingency amount to reflect a current assessment of the eventual outcome. The forecast final costs at each review period then include an updated forecast of how much of the contingency amount is likely to be expended.

Direct cost items

With regard to direct costs (e.g. direct labour), the historical accounting process has traditionally been in trouble as an indicator of the true situation because of the "percentage complete problem" (see Stretton 2009f). This is not the fault of the accounting system per se, but more of project management.

The best approach I know of to overcoming this problem is for the project manager to use the Work Breakdown Structure to break down each work item into units whose durations are not greater than the formal cost control review periods, as discussed in more detail in Stretton 2009f. If this is done, each such unit of the item is either completed at review time, or has not yet started, or is in progress.

In the latter case, a slightly incorrect assessment of the unit's percentage completion in the review period will be insignificant in the context of evaluating the item's overall project cost position.

An effective approach for cost control of direct cost items is then to forecast the final position for each, taking into account actual performance of completed units to date. The forecast final cost is compared with the budgeted cost for that item. Movements of forecast final variance from the budgeted cost are then analysed, to help identify items that may need current remedial action.

IN SUMMARY

This short commentary has discussed some legitimately conflicting differences in perception and practice between project managers and accountants in relation to cost and financial management of projects, and some steps to help overcome them.

With regard to project costs, conventional accounting practices which record costs when payment is made are of course vital, but are not sufficient on their own to effectively control cash flow or project costs. Both of the latter need forecasting capabilities, which suggests using a separate control system which facilitates such forecasting. Attributes of the latter were discussed in the context of commitment costing for procurement items, and very specific WBS breakdowns for non-procurement items.

There is an obvious need to reconcile the conventional accounting system with the project control system. Amongst other things, this requires mutual understanding of the legitimately different perspectives of accountants and project managers.

REFERENCES

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Alan Stretton is one of the pioneers of modern project management. He is currently a member of the Faculty Corps for the University of Management & Technology (UMT), USA. In 2006 he retired from a position as Adjunct Professor of Project Management in the Faculty of Design, Architecture and Building at the University of Technology, Sydney (UTS), Australia, which he joined in 1988 to develop and deliver a Master of Project Management program. Prior to joining UTS, Mr. Stretton worked in the building and construction industries in Australia, New Zealand and the USA for some 38 years, which included the project management of construction, R&D, introduction of information and control systems, internal management education programs and organizational change projects. He has degrees in Civil Engineering (BE, Tasmania) and Mathematics (MA, Oxford), and an honorary PhD in strategy, programme and project management (ESC, Lille, France). Alan was Chairman of the Standards (PMBOK) Committee of the Project Management Institute (PMI®) from late 1989 to early 1992. He held a similar position with the Australian Institute of Project Management (AIPM), and was elected a Life Fellow of AIPM in 1996. He was a member of the Core Working Group in the development of the Australian National Competency Standards for Project Management. He has published over 140 professional articles and papers, many of which can now be found in the PM World Library. Alan can be contacted at alanailene@bigpond.com.au.